

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 2003-6-G – ORDER NO. 2003-641
OCTOBER 24, 2003

IN THE MATTER OF:

South Carolina Pipeline Corporation -)
Annual Review of Purchased Gas)
Adjustments (PGA) and Gas Purchasing)
Policies)
_____)

ORDER RULING
ON PETITIONS

This matter comes before the Public Service Commission of South Carolina (“Commission”) on the Petition for Rehearing and/or Reconsideration filed by the Consumer Advocate for the State of South Carolina (“Consumer Advocate”) in which the Consumer Advocate requests that we rehear and/or reconsider our decision in Order No. 2003-489 denying his motion seeking to modify the terms of the Industrial Sales Program Rider (“ISP-R”) by requiring South Carolina Pipeline Corporation (“SCPC” or “Company”) to assign to its interruptible customers the highest cost gas at which SCPC can still make the sale. The Company and Commission Staff each filed a responsive pleading opposing the Consumer Advocate’s Petition.

This matter also comes before the Commission on the Petition for Rehearing and/or Reconsideration on the Existing Record filed by the Company in which the Company requests that we rehear and/or reconsider our decision in Order No. 2003-489 to “. . . hold in abeyance any decision on the recovery of the use of put options until such time as a generic proceeding can be held concerning SCPC’s utilization of puts and other financial devices.” The Company also

requests in its Petition that we issue a ruling on reconsideration that the Company's purchase of put option contracts connected to the purchase of physical gas supplies during the review period was reasonable and prudent. No responsive pleading was filed in opposition to the Company's Petition. For the reasons set forth below, we (i) deny the Consumer Advocate's Petition, (ii) grant the Company's Petition, and (iii) find that the Company's purchase of put option contracts during the review period was reasonable and prudent.

I. CONSUMER ADVOCATE'S PETITION

In Order No. 2003-489, we approved the continuation of the Company's ISP-R without modification, and we denied the Consumer Advocate's motion to modify the ISP-R to require the Company to assign gas to its interruptible customers with the highest cost with which the Company could still make the gas sale. The principal basis for our decision in Order No. 2003-489 was that there was not enough evidence in the record for us to consider properly the Consumer Advocate's motion. The Consumer Advocate argues in his Petition that we erred in holding that there was not enough evidence in the record to consider properly his motion, and that our failure to grant his motion results in gas costs and rates for firm customers, which are unjust, unreasonable and discriminatory. We find both of the Consumer Advocate's arguments to be unpersuasive, and, therefore, deny his request for rehearing and/or reconsideration.

In 1983, the Commission approved the Company's ISP-R,¹ and for nearly twenty (20) years thereafter, the Commission has consistently found, when the issue has been presented for consideration, that the ISP-R benefits SCPC's pipeline system as well as its firm and sale-for-resale customers. Accordingly, as a matter of law, the ISP-R and its policies are presumptively correct. *See Hamm v. S.C. Pub. Serv. Comm'n*, 315 S.C. 119, 432 S.E.2d 454 (1993).

¹ See Order No. 83-222; *see also* Order No. 83-873.

Therefore, any party such as the Consumer Advocate, who attempts to challenge SCPC's right to continue the program, bears the burden of proof in attempting to establish that this longstanding program approved by the Commission requires modification.

The Consumer Advocate argues in his Petition that the goals of the ISP-R could still be attained even if SCPC were required to modify the ISP-R to assign gas to its interruptible customers, on an individual basis, with the highest cost with which the Company could still make the sale. However, at the hearing the Consumer Advocate offered no fact witnesses, no expert witnesses, and no documentation. In short, the Consumer Advocate offered no evidence in support of his proposed modification. Instead, the Consumer Advocate relies solely upon the cross-examination testimony of Commission Staff witness Brent L. Sires as elicited by the Consumer Advocate. The Consumer Advocate argues that because Sires agreed that the goals of the ISP-R would be retained even if the Company were required to modify the ISP-R to assign gas to its interruptible customers with the highest cost with which the Company could still make the sale, Sires' statement constitutes sufficient evidence to warrant a modification of the Company's ISP-R. We disagree.

A full and fair review of the record reveals that the Consumer Advocate is relying upon a single passage of Sires' testimony, which is taken out of context. This isolated and out-of-context question and answer does not accurately and fully explicate or reflect the thrust of Sires' testimony. To the contrary, a complete and comprehensive review of the entire record reveals that Sires opined that the Company's ISP-R as structured and operated over the past twenty (20) years is necessary for the Company to compete effectively with alternate fuels in the industrial market. TR.p.188. Moreover, the record clearly reflects that Sires recommended to the Commission that the Company's ISP-R be continued in its current form without modification.

TR.p.188. In summary, witness Sires' testimony, when taken as a whole, does not support the Consumer Advocate's assertion that the ISP-R should be modified, therefore, we deny the Consumer's Advocate's Petition based upon this argument.²

In further support of the Consumer Advocate's Petition, the Consumer Advocate argues that our failure to grant his motion results in gas costs and rates for firm customers, which are unjust, unreasonable and discriminatory. In an attempt to explain his argument, the Consumer Advocate states in his Petition,

Under the ISPR program, gas supplies which are not directly assigned to direct industrial interruptible customers are available to be included in the pool of gas which makes up the Weighted Average Cost of Gas (WACOG). Firm customers, such as sale-for-resale customers like SCE&G, pay the WACOG price for gas, which is then sold to residential and small business customers. Assigning most of the lowest price gas to ISPR customers results in higher priced gas being assigned to the WACOG. That means higher gas prices for residential and small business customers.

² In further support of our ruling, we cannot ignore the uncontradicted and undisputed testimony of SCPC witness Samuel L. Dozier. In fact, at no time during the hearing did any party to the proceeding challenge or discredit the testimony of Mr. Dozier concerning the benefits realized as a direct result of the ISP-R. Specifically, Dozier testified that during the review period the ISP-R continued to provide the Company with a degree of operational and cost stability for the firm market that could not be met by any other means. TR.p.37. Dozier also testified that because the ISP-R allows the Company to maintain competitive sales to industrial customers with alternative fuel sources, the Company is able to make sales to interruptible customers that otherwise might not be made. TR.pp.37-38.

We find that there are a number of benefits realized by the Company's customers, which are directly attributed to the ISP-R. For example, because service provided to the ISP-R customers is interruptible, SCPC can curtail this service when it needs to use the transportation capacity and gas supply to satisfy firm customer demands. TR.p.38. In addition, the ISP-R allows SCPC to earn margins from competitive industrial customers that pay a substantial portion of SCPC's fixed costs, costs that would otherwise be paid by the firm customers. TR.p.38. Accordingly, we find that without the ISP-R margins, those costs would have to be paid by the firm customer classes, namely the Company's residential and commercial end users. In sum, as it is structured today, we find that the ISP-R provides for pricing flexibility, enhances system reliability, and contributes to system revenues and price stability. TR.pp.38-39.

(Consumer Advocate's Petition at p.4).

When the Commission approved the ISP-R in 1983, we expressly acknowledged in Order No. 83-222 our responsibility to regulate natural gas services and rates provided by the Company to benefit the public interest. Thus, we considered the impact that the then proposed ISP-R would have upon all classes of customers and not just upon the participants of the ISP-R. In deciding whether to implement the ISP-R, we specifically found that all of the Company's customers would directly benefit from the ISP-R. *See* Order No. 83-222. Moreover, in Order No. 83-873 we stated that “. . . the beneficial effects of the [ISP-R] should reach all categories of natural gas users in the Company's service area.”

This Commission's precedent makes clear that at the time we approved the ISP-R, the ISP-R did not produce unjust, unreasonable and discriminatory gas costs. In fact, among other reasons, we approved the ISP-R because it provided benefits to all customer classes, and this reasoning remains true today. Because the Consumer Advocate has not presented the Commission with any evidence to convince us otherwise, we find that the ISP-R continues to benefit all customer classes, and therefore, does not produce unjust, unreasonable and discriminatory gas costs.

In Order No. 83-222, we found that, “the margin received by the Company pursuant to [the ISP-R] will help pay the fixed cost that would be paid by the Company's non-qualifying industrial gas customers and the firm resale distributor companies.” Through our approval of the ISP-R, we concluded that “[t]he rates for natural gas services paid by natural gas customers, other than [ISP-R] customers, of the Company will be the same or lower as that rate which would have been paid had the deliveries of natural gas to the [ISP-R] customers not been made.”

See Order No. 83-222. Accordingly, we find that the rate of return earned by the Company from sales conducted under the ISP-R is used in part to benefit all customer classes of SCPC.

We further find that the Consumer Advocate's argument is based solely upon conjecture and speculation and is without any evidentiary support. Instead of evidence, the Consumer Advocate relies upon a conclusory statement as support for his request that we modify the Company's ISP-R. As a matter of law, however, a conclusory statement based upon speculation and conjecture is no evidence at all and is legally insufficient to support the Consumer Advocate's attempt to convince us that the ISP-R should be modified.

At no point during the Company's PGA proceeding did the Consumer Advocate present any evidence demonstrating that the ISP-R produced discriminatory rate differences between customer classes. In fact, the Consumer Advocate did not present any evidence at all in support of his argument or any evidence to cause this Commission to make a ruling contrary to Commission precedent. Moreover, the Consumer Advocate failed to elicit any testimony from any witness at the hearing that even hinted at the prospect that the ISP-R produced discriminatory rate differences between customer classes. There is substantial, sufficient, and adequate evidence contained in the record clearly showing that any decision by the Commission other than continuing the ISP-R without change would be arbitrary and capricious and detrimental to SCPC and its residential and commercial customers. Accordingly, we deny the Consumer Advocate's Petition for reconsideration wherein he alleges that our failure to grant his motion results in gas costs and rates for firm customers, which are unjust, unreasonable and discriminatory.

As a concluding remark in his Petition, the Consumer Advocate states that “. . . we should open a proceeding to examine the continuation of the ISPR where all evidence is available and relevant to the inquiry.” [Consumer Advocate’s Petition at p.5]. However, the Consumer Advocate presented no evidence whatsoever which would warrant the institution of such a proceeding. We find that our annual review of the Company’s PGA and Gas Purchasing Policies serves as an appropriate vehicle in which to evaluate the Company’s ISP-R. Therefore, we deny the Consumer Advocate’s request that we open an additional proceeding to examine the continuation of the Company’s ISP-R.

In sum, the Consumer Advocate has failed to convince us that we should rehear and/or reconsider our decisions concerning the denial of his motion related to the Company’s ISP-R. Therefore, for the reasons stated above, the Consumer Advocate’s Petition is hereby denied and dismissed.

II. THE COMPANY’S PETITION

In Order 2003-489, we held “. . . in abeyance any decision on the recovery of the use of put options until such time as a generic proceeding can be held concerning SCPC’s utilization of puts and other financial devices.” SCPC now seeks reconsideration on the existing record of this decision by arguing in its Petition that it would be “a grievous error of law” for the Commission to hold a generic proceeding on the Company’s use of put option contracts and then retroactively apply any decision or ruling to the Company’s use of put options during the period under review. The Company also argues that the Commission is required by law to issue a ruling based solely upon the testimony and evidence accepted into the record. As stated above, no responsive pleading was filed opposing the Company’s Petition.

After careful review and consideration of the arguments and applicable legal authority set forth in the Company's Petition, we hereby grant the Company's Petition and reconsider on the existing record our previous decision. For the reasons stated below, we now rule, based upon the testimony and evidence presented to us at the PGA proceeding, that the Company's purchase of put option contracts during the period under review was reasonable and prudent.

A. STANDARD OF REVIEW

Initially, we note that the Company's purchase of put option contracts resulted in additional costs being borne by sale-for-resale customers in the price of the weighted average costs of gas ("WACOG"). This fact, however, does not control our decision as to whether the Company's purchase of put option contracts was reasonable and prudent because our evaluation of prudence does not end with simply determining whether a particular decision results in additional costs to the price of gas. Rather, our review of prudence focuses on the material facts and circumstances surrounding the Company's decision at the time the Company made the decision being reviewed. Therefore, our determination of whether the Company's decision to purchase put option contracts was reasonable and prudent is based upon the information available to the Company at the time it purchased the put option contracts. Accordingly, in our review of the Company's PGA and Gas Purchasing Policies we do not scrutinize the Company's decisions and actions based upon hindsight. To the contrary, our review of the Company's PGA and Gas Purchasing Policies is based upon the information that the Company knew at the time it made the decision to purchase the put option contracts.

B. FINDINGS OF FACT AND CONCLUSIONS OF LAW

Based upon the record before us, we find that the Company's decision to purchase put option contracts was reasonable and prudent. No party to the proceeding presented any evidence

contrary to this finding. In March 2002, the Company purchased 920 put option contracts to take advantage of an up-tick in NYMEX prices to offset the possible effect of the price of gas included within the WACOG. TR.p.103; p.168. In support of its decision to purchase put option contracts, the Company presented the testimony of Kevin B. Marsh, who explained the Company's reasoning for purchasing the put option contracts.

Marsh testified that a put option contract is an industry-recognized tool widely used to manage gas cost, and that the put option contracts functioned as protection for the Company's customers in the event that natural gas prices declined. TR.p.254; p.261. Marsh testified that the Company's decision to purchase the put option contracts in the spring of 2002 was made on an individual-case basis and incorporated the collective opinions of the Company's management. TR.p.274-75. Marsh also testified that the Company's decision to purchase the put option contracts was based upon the best market information available to the Company at the time the purchases were made. TR.pp.261-62.

At the hearing, Marsh also explained the Company's decision-making process prior to purchasing the put option contracts. Marsh testified that the Company monitors the natural gas market on a regular basis, and that the Company has regular contact with natural gas producers, suppliers, and a number of industry analysts. TR.pp.262-63. Marsh testified further that the Company's "... general experience and knowledge level of buying gas for the years we've been in the business provides [the Company] ... with a level of expertise to help us evaluate when might [be] the appropriate time to purchase a put option or other instruments that might be out there." TR.p.263. Additionally, after the Company collected the necessary information concerning the purchase of put option contracts, the Company's purchasing group presented the information to its risk management committee who, in turn, analyzed, reviewed, and discussed

the information prior to making the decision to purchase the put option contracts. TR.p.274. Moreover, Commission Staff witness Sires testified that from his audit and review of the Company's purchasing practices for the period under review, it was his opinion that the Company's purchasing practices, including the decision to purchase put option contracts, was prudent. TR.p.232.

There is adequate and sufficient evidence contained in the record explaining the market conditions that confronted the Company when it decided to purchase the put option contracts at issue and that the put option contracts functioned as intended by providing insurance protection against the risk of price volatility on the downside. In addition, there is substantial and uncontradicted evidence contained in the record supporting the Company's decision to purchase the put options contracts. Therefore, based upon the testimony and evidence contained in the record before us, we find that the Company's purchase of put option contracts was reasonable and prudent, and that it was appropriate for the Company to recover the costs of the put option contracts through the WACOG.

IT IS THEREFORE ORDERED THAT:

1. The Consumer Advocate's Petition for Rehearing and/or Reconsideration is denied and dismissed.
2. The Company's Petition for Rehearing and/or Reconsideration on the Existing Record is granted.
3. The Company's decision and purchase of put option contracts was reasonable and prudent, and the costs of such contracts were properly recovered through the WACOG.
4. All other issues addressed by Order No. 2003-409 and not discussed herein are not disturbed by this Order.

5. This Order shall remain in full force and effect until further order by the Commission.

BY ORDER OF THE COMMISSION:



Mignon L. Clyburn, Chairman

ATTEST:



Bruce Duke, Acting Executive Director

(SEAL)